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Abstract

The sovereign debt crisis induced a wide array of new institutions to reinforce European economic governance. The budget of the European member states is now subject of the European semester, which is part of the preventive arm of the Stability and Growth Pact as codified by and backed-up by the so-called Six-Pack and Two-Pack and backed by the Fiscal Compact that enable the Commission to issue, inter alia, country-specific recommendations before the budget is submitted to national parliaments. The country-specific recommendations are not binding, but will be hard to ignore by the member states in the long run unless the economy recovers.

In this paper we are going to look at the efforts of the European Union to reinforce European fiscal governance, i.e. the coordination of the budgetary policy of the member states. More precisely, we will address the progress of the member states towards their Medium-Term Budgetary Objective as measured by the structural balance and Expenditure Benchmark as well as the implementation of the Country-Specific Recommendations in the field of fiscal policy, which are further strengthened by the Fiscal Compact by which the member states – with the exception of the Czech Republic and the United Kingdom – commit themselves to fiscal discipline, coordination and governance.

The paper is geared to the assessment the country-specific recommendations in terms of goal-attainment and effectiveness and aims, by such, to deliver a contribution to the body of knowledge on European economic governance and fiscal consolidation.

Keywords

European Governance, Fiscal Policy, Stability and Growth Pact, Overall Assessment, Country-Specific Recommendations

Acknowledgement

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Acronyms

BEPG:	Broad Economic Policy Guidelines
COREPER:	Committee of the Permanent Representatives of the Member States
CR:	Country reports
CSR:	Country-Specific Recommendations
CSR-1:	Country-Specific Recommendations in the field of public finance
DBP:	Draft Budgetary Plans
DG ECFIN:	Directorate-General for Economic and Financial Affairs
EB:	Expenditures Benchmark
ECB:	European Central Bank
ECOFIN:	Economic and Financial Affairs Council
ECON:	Economic and Monetary Affairs Committee
EDP:	Excessive Deficit Procedure
EFC:	Economic and Financial Committee
EMU:	Economic and Monetary Union
EP:	European Parliament
GDP:	Gross Domestic Product
MTO:	Medium-Term Budgetary Objective
NRP:	National Reform Programs
OA:	Overall Assessment
SDP:	Significant Deviation Procedure
SGP:	Stability and Growth Pact
SCP:	Stability and Convergence Programs

1. Introduction

The sovereign debt crisis induced a wide array of new institutions to reinforce European economic governance. The budget of the member states is now subject of the European semester, which directs the coordination of the budgetary policy of the member states[1]. It enables the Commission, inter alia, to issue country-specific recommendations [CSR] before the budget is submitted to national parliaments. The country-specific recommendations may not be binding, but will be hard to ignore by the member states in the long run unless the economy recovers. In this paper we will address the question if the efforts to reinforce the preventive arm of the SGP and, more precisely, the CSR in the field of fiscal policy have been successful in terms of fiscal consolidation. As they are based on the assessment of the Stability and Convergence Programs [SCP] that the member states have to submit in the spring and the Draft Budgetary Programs [DBP], which are due in the fall, we will pay due attention to the overall assessment by the Commission of the fiscal performance of the member states as measured by their tailor-made Medium-Term Budgetary Objectives [MTO] and the Expenditure Benchmark [EB], before we look at the compliance of member states with the CSR, notably in the field of fiscal policy[2]. The focus is on the Euro area.

The paper is organized in seven sections. We start with the current debate about European fiscal governance [section 2]. Next, we address then the new architecture of the SGP that originally dates from the Amsterdam summit on June 16-17, 1997. Since the SGP has gone through two major reforms. The first was due to the Council decision to impose no sanctions on France and Germany, although they were in derogation for two years in a row. The second refers to the consequences of the sovereign debt crisis [section 3]. One of the novelties was introduction of the European semester, which is codified by the Six-Pack and Two-Pack. The latter introduced, inter alia, a common budgetary timetable [section 4]. We precede then with the preventive arm of the SGP and more precisely the overall assessment of the performance of the member states [section 5] before we look at the country specific recommendations [section 6]. The paper is complete with a discussion about the role of the Commission in the architecture of the SGP and the impact of the CSR on fiscal consolidation [section 7].

2. European Fiscal Governance

The paper is aimed at a contribution to the academic and professional debate about European governance and, more precisely, the reinforcement of European economic governance in response to the sovereign crisis. Taking the tripartite model of Wessels en Linsenmann as a point of reference [Wessels & Linsenmann 2002: 55], the focus is primarily on fiscal policy. However, the interaction effects with the monetary policy, respectively economic [read: structural] policy should not be overlooked. The design of the EMU is heavily criticized for its asymmetry between its centralized monetary policy and decentralized fiscal policy [Verdun 1996; Jabko 2011]. In a way it constitutes a paradox [Hodson 2013]. On the one hand, the SGP has been surprisingly resilient. On the other hand, it could be held responsible for the slow response of the European Union to the sovereign debt crisis [Hinarejos 2015: 13-

1. The European semester is part of the preventive arm of the Stability and Growth Pact [SGP] as codified by the so-called Six-Pack and Two-Pack and backed-up by the intergovernmental Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, better known as the Fiscal Compact.
2. In this paper budgetary policy and fiscal policy are used interchangeably, although the latter is a broader concept as it also refers to the stimulation of the economy.

14]. In fact, the Five Presidents' Report is exactly geared towards the correction of what is considered to be a flaw in the institutional set-up of the EMU as confirmed, once again, by White Paper on the Future of Europe [Junker 2015; Junker 2016]. One may argue though that the – internal and external – track record of the euro is not so bad after all and that the monetary union does not, at least not necessarily, requires a fiscal union [Wren-Lewis 2013]. On the contrary, one may even call for a decentralization of both the design and the implementation of fiscal rules without questioning the importance for fiscal discipline [Wyplosz 2015: 26].

The body of knowledge on European economic governance has got new impulse lately from two new strands of literature.

1. The academic debate on 'new intergovernmentalism', which is centered around the so-called 'integration paradox', i.e. the pursuit of European integration or rather cooperation without further supranationalism [Puetter, 2012: 168; Bickerton et al. 2015: 705; Fabbrini & Puetter 2016: 485]. Although one may question if new intergovernmentalism is mere old wine in new bottles [Schimmelfennig 2015] we would argue that the integration paradox has worked exactly in the opposite direction in the case of European fiscal governance. The outcome of the latest reform of the SGP may be characterized best by 'new supranationalism' [Dehousse 2015] as the Commission is equipped by all kinds of new instruments. However, these new tools are provided by the member states, pointing at a co-existence of both interpretations of the current state of European integration [Schmidt 2017].
2. The establishment of a new architecture of 'experimentalist governance', which is based on a co-production by the European institutions and the member states of rather broad frameworks in terms of goals and metrics, leaving the implementation basically to the discretion of the member states in exchange for periodically reports on their performance[3]. Although the evolution of European fiscal governance may not characterized as experimentalist [Zeitlin 2016: 1091, note 3] it could be useful as a heuristic tool to get a better insight in the modus operandi of European fiscal governance. Even more importantly, policy makers seem to have learned a lesson by looking at modes of soft coordination, calling for a more flexible interpretation of rules, to accomplish their goals[4]. The outcome is a hybrid mode of European fiscal governance, composed of a combination of rule-based and coordination-based forms of governance [Armstrong 2013: 15].

In the remaining of this paper we will focus on the new architecture of the SGP with regard to the coordination of the budgetary policy of the member states. Special attention will be paid to the overall assessment by the Commission of the fiscal performance of the member states as measured by their MTO and EB as well as the design and implementation of the CSR in the field of fiscal policy.

3. The performance of the member states is subject to a peer review. The outcome is compared with those others following different means towards the same ends. The system is regularly updated in response to the problems and options revealed by the review process [Zeitlin 2016: 2].
4. It may be even argued that the shadow of soft coordination makes fiscal surveillance more effective as hard fetters are crippling and may simply break while somewhat elastic ties give some room for maneuvering while still being resilient [Schelkle 2007: 730].

3. The New Architecture of the Stability and Growth Pact

3.1 The First Reform of 2005

The first reform of the SGP dates back to November 25, 2003 when a proposal of the Commission to impose sanction on France and Germany was effectively vetoed by a blocking minority of the large countries[5]. The decision was challenged by the Commission, supported by a number, but not all small countries, when it filed legal action on January 13, 2004. On July 13, 2004 the Court delivered a Solomonic verdict. On the one hand, it ruled that the ECOFIN acted illegally when it drew conclusions that were *not* based on a recommendation of the Commission and, by such, put the threat of sanctions into abeyance [Bailey & Kirkegaard 2004: 253-254]. On the other hand, it ruled that the ECOFIN does not have to follow the recommendations of the Commission to impose sanctions. Consequently, no sanctions were imposed on France and Germany, but instead the Court ruling induced a change in the rules of the game [Heipertz & Verdun 2010: 163].

The first reform of the SGP basically made it country-specific by taking into account the economic characteristics of each country. The reference value of the budget deficit and public debt was kept in place, but the differentiation of the MTO, measured in terms of the structural balance net of one-off and temporary measures, effectively replaced the actual deficit by the structural balance as the main yardstick to assess budgetary performance. In addition it introduced all kinds of new exception clauses, which explains why the reform of the SGP of 2005 is generally considered as a softening [Schelkle 2007: 709]. However, a couple of nuances seem to be appropriate. First, a distinction can be made between three dimensions of governance, i.e. obligation, delegation and precision. A closer look at the reform of the SGP of 2005 reveals that the obligations are weakened indeed, but that delegation and precision have been strengthened [Schelkle 2007: 712]. Arguably, it made the SGP better equipped to deal with the contingencies of fiscal policy by emphasizing the procedural rather than the substantial aspects of fiscal governance. Second and even more importantly, the reform of the SGP introduced cyclical adjustment in the monitoring of the public finances in the member states, which constitutes de facto a strengthening rather than a weakening [Pisani-Ferry 2014: 54]. By taking out the impact of the economic cycle a better view is provided on the taxing and spending behavior of the government of the member states.

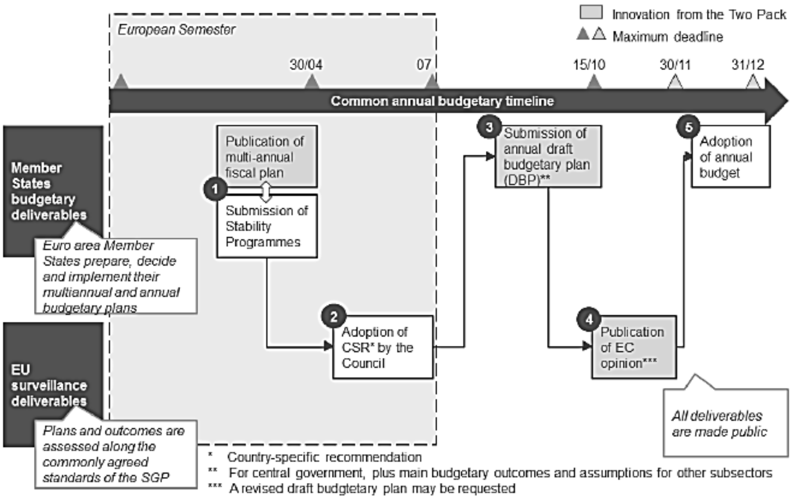
3.2 The Second Reform of 2011

The second reform of the SGP was largely due to the consequences of the sovereign debt crisis that hit the European Union due to the Greek tragedy. One of the main innovations, although not completely new, was the introduction of a so-called European Semester by a Task Force on Economic Governance in the European Union, chaired by the newly appointed president of the European Council, Herman van Rompuy, who skillfully used the anti-supranational mood of that time to take the initiative [Hodson & Puetter 2013: 367; Fabbrini 2016: 245][6]. A detailed account of the proceedings of the Taskforce is delivered by Michele Chang, providing insight in the internal dynamics of the Taskforce as well as the power game

5. A number of three small countries – Ireland, Luxembourg and Portugal – supported the large countries for various reasons [Heipertz & Verdun 2010: 149-153].
6. The composition of the Taskforce largely mirrored the Council in the composition of the Ministers of Finance.

between the Taskforce and the Commission [Chang 2013], which was effectively sidelined as the preparatory work was carried out by the so-called Sherpa's, a group of senior civil servants from the member states [Puetter 2014: 118; Puetter 2015: 179]. However, the situation is more balanced as the whole idea of the European semester is deeply rooted in the Commission [European Commission 2010: 258; Dehousse 2015: 12]. Besides, the Commission shaped the agenda at least twice – on May 12 and on June 30 – by issuing statements ahead of a meeting of the task force. In both statements attention is paid to the introduction of a European semester. In an effort to regain the lead in the field of European economic governance the Commission tabled the so-called Six-Pack – five regulations and one directive – one month ahead of the adoption of the Van Rompuy report [Pisani-Ferry 2011: 110, fn. 5]. In fact, one may argue that the Six-Pack basically codified the European semester [Laffan & Schlosser 2015: 3][7]. The reform of the SGP is completed by the adoption of the Two-Pack, backed-up by the Fiscal Compact, which direct the coordination of the budgetary policy of the member states. The outcome is clearly supranational as it equipped the Commission with new tools[8].

Figure 1: *The Common Budgetary Timeline*



Source: EC, Public Finances in EMU 2013: 85

The reform of the SGP brought the coordination of fiscal policy and structural policy together in an overall, more coherent framework, the European semester, refining and streamlining the procedures that were already in place, introducing semi-automatic sanctions in both arms of the SGP led by a reserve voting mechanism[9] and, above all, expanded the domain of the SGP to reduction of macroeconomic imbalances. In this paper we will mainly look at the preventive arm of the SGP reforms regarding the coordination of budgetary policy. In a communication the Commission stated that the time was ripe for a

7. The six-pack is issued on September 29, 2010, while the Van Rompuy taskforce reported on October 21, 2010.
8. A similar conclusion is drawn by Isabel Camisão in her analysis of the role of the Commission during the sovereign debt crisis [Camisão 2015: 282].
9. A proposal for automatic sanctions is traded-off for a change of the 'no bailout clause' [TFEU, Article 125] at informal gathering of Angela Merkel and Nicolas Sarkozy at Deauville on October 18, 2010 at the very moment that the Van Rompuy taskforce met in Luxembourg to finalize its report [Chang 2013: 166; Van Nispen & Rijk 2014: 15].

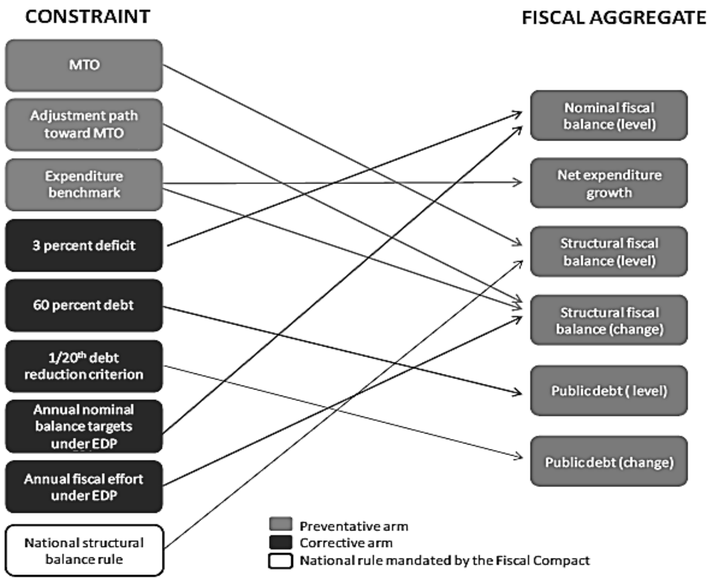
budgetary and economic surveillance *ex ante* on the principle that 'prevention is more effective than correction' [COM (2010) 250 Final: 8].

The reform of the SGP, inter alia, set a new timeline for the submission of the SCP so that they 'not only codify, but may also modify the fiscal plans for coming year' [Van Nispen 2011: 12; Van Nispen & Rijk 2014: 14][10]. In addition, it introduced the assessment of the DBP by Commission before the start of next fiscal year. We will follow the new timeline, which is composed of five place-marks [Figure 1]. In addition, the reform of the SGP empowered the Commission to issue Country-Specific Recommendations [CSR] on top of the Broad Economic Policy Guidelines [BEPG], which serve as the basis for the assessment of the SCP and NRP [Degryse 2012][11]. Consequently, the CSR cannot properly be understood without the assessment of the SCP [and NRP] by the Commission as part of the European semester. As the submission of the DBP only applies to the member states that adopted the single currency we will focus on the countries in the Euro area.

4. The Coordination of the Budgetary Policy

The assessment of the budgetary policy of the member states has become rather complex, due to continuous fine-tuning of the rules[12]. A useful overview of the fiscal rules that are in place is provided by Eyraud & Wu [2015: 15], linking the constraints imposed by these fiscal rules to the main indicators used by the Commission to assess the performance of the member states [Figure 2].

Figure 2: *Supranational Constraints and Rules on Fiscal Aggregates*.



Source: Eyraud & Wu 2015: 15; Andrle et al. 2015: 9.

10. The SCP are now due in the spring. In the past recommendations came often too late as the SCP were due in the fall, '… simply reporting what they have already passed into law' [Hallerberg 2010: 8].
11. The current BEPG are geared towards the goals of the Europe 2020 strategy.
12. In addition a considerable extension has taken place of budgetary information to be provided by the member states [Schelkle 2009: 834].

The large number of indicators – targets, upper limits, and benchmarks for the nominal balance, structural balance, expenditure growth and debt developments – make it extremely difficult for national governments to oversee all the consequences of the system, not to say to deliver an adequate and coherent response [Presidency Note 2016]. The annual update of the *Vade Mecum on the Stability and Growth Pact* is a step in the right direction, but it is still difficult, notably for outsiders, to trace the opinion of the Commission as not all data and underlying calculations are made public[13]. In an effort to reduce the complexity of the current fiscal rules and to make the system more predictable and more transparency the Commission has announced a plan that, inter alia, will streamline the methodology for assessing compliance with the requirements under the preventive, respectively corrective arm of the SGP by reliance on a single practical indicator [COM(2015) 600 final], i.e. the expenditure benchmark.

A more comprehensive proposal to drop the structural balance and to focus on the expenditure rule is provided by Claeys et al. who argued, inter alia, in favor of the measurement of aggregate expenditure, which is now corrected by the forecast of the GDP deflator, in nominal instead of real terms. In addition, the expenditure benchmark should be supplemented with an inflation target of 2 percent for countries in the euro area. Furthermore, a debt-feedback mechanism should make the 1/20th debt reduction rule redundant [Claeys et all 2016][14]. A couple of months ago the ECOFIN decided, having consulted the EFC, to settle at a less far reaching simplification of the rules, which may be considered, at best, a second-order change [Hall 1993] [15]. The structural balance is kept in place [ECOFIN 2016] basically due to the fact that it is anchored in the German constitution. In practice, though, we may feature a shift away from the structural balance, becoming gradually obsolete, to the expenditure benchmark as the latter is considered a more operational and easier to measure indicator and, as such, may guide the member states in the preparation as well as the monitoring of the execution of the annual budget.

5. The Preventive Arm of the Stability and Growth Pact

The performance of the member states is assessed by the Commission with the help of a refined, but complicated model, which is based upon two pillars[16]. The first pillar consists of the assessment of the Medium-Term Budgetary Objective [MTO] in terms of the structural balance, which is defined as the actual [or headline] deficit, adjusted for the cycle and excluding one-off and other temporary measures [Vade Mecum 2016: 26]. The second pillar involves an analysis of compliance with the expenditure benchmark [EB], which sets an upper

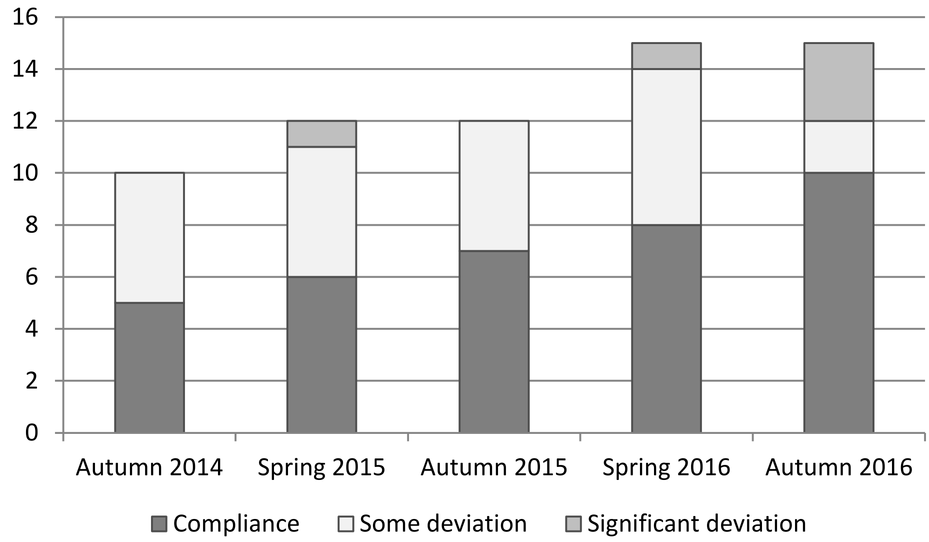
13. The data and calculations underlying surveillance decisions are only shared by the Commission with the national authorities [Commission 2016: 1].
14. A similar proposal is done by the IMF calling for a single fiscal anchor with a single operational rule [Andrle et al.2015].
15. The introduction of the expenditure benchmark in the careful analysis, which is part of the corrective arm of the SGP, is the main novelty. It aims at simplifying the assessment of compliance with EDP recommendations and increasing the consistency with the preventive arm of the SGP.
16. In addition, the debt criterion is taken into account. Furthermore, member states coming out the corrective arm of the SGP are subject of the debt rule during a transition period of three years in order to ensure that they have time to adapt their structural adjustments to the level needed to comply with the debt reduction benchmark [Vade Mecum 2016: 145].

limit for the net growth of public expenditures. They lead, combined together, to the so-called overall assessment of fiscal performance of the member states.

5.1 Medium-Term Budgetary Objectives

The performance of the member states ex ante is assessed twice a year. First in the spring as part of the assessment of SCP, cumulating into in the adoption of CSR and second in the fall as part of the analysis of DPBs, leading to a Commission opinion about next year's budget[17]. The system takes the MTO, which are updated every three years, as the point of departure. First, the Commission will check if the MTO has been attained[18] in previous year [t-1] and, if not, whether that country is on an appropriate adjustment path, which is set at an annual improvement of the structural balance by 0.5% of GDP as a benchmark for member states with a debt below the reference rate of 60% of GDP. A faster adjustment path, i.e. more than 0.5% of GDP, is applicable to member states with debt in excess of 60% of GDP or with pronounced risks of overall debt sustainability [Vade Mecum 2016: 37]. The compliance of the member states with the MTO in the Euro area is provided in Figure 3, based on in-year data and one year deviation from the required adjustment[19].

Figure 3: *Compliance with the Medium-Term Budgetary Objectives, Euro Area* [FY 2014-2016] [20].



Source: SCP and DBP, FY 2014-2017 [own calculations]

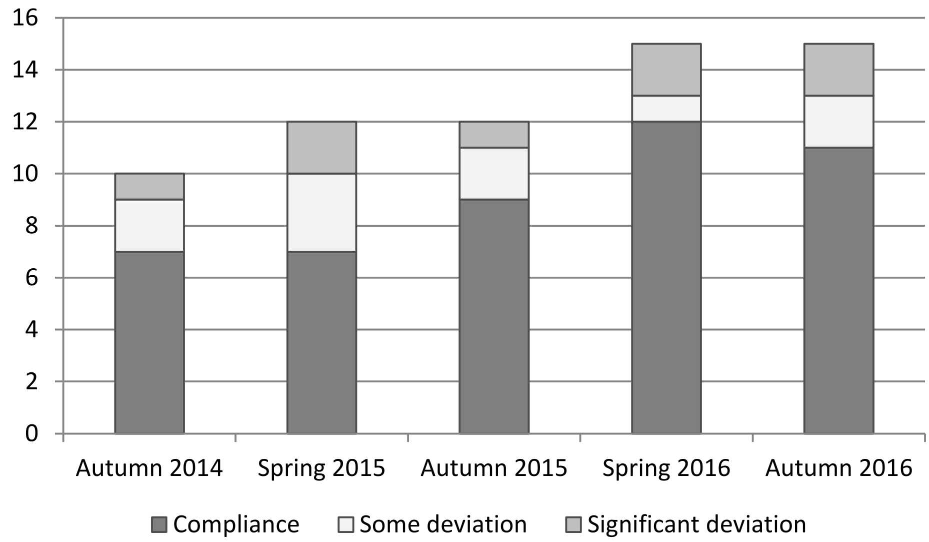
17. Contrary to the assessment of the SCP, which is adopted by the ECOFIN, the assessment of the DBP is left to the Commission, which should issue an opinion before November 30.
18. The MTO are updated every three years, or more frequently in the case a Member State has undergone a structural reform significantly impacting its public finances.
19. A deviation from the required adjustment for countries, which are not yet at their MTO, is considered not significant if the deviation is less than 0.5% of GDP in a single year or 0.25% of GDP on average per year in 2 consecutive years [Vade Mecum 2016: 53].
20. The performance of the member states is visualized with the help of a color system, mirroring a traffic light. It is used for the first time to assess the SCP of 2015.

The track record of the MTO is poor [ECB 2015: 57]. Contrary though the findings to the ECB we feature a positive trend of the number of member states that is ‘at or above’ their MTO [Figure 3], although the deadline for the accomplishment of the MTO is advanced indeed to the future. The compliance to the MTO is currently at risk in 3 out of 15 member states in the Euro area under the preventive arm – Belgium, Ireland and Slovenia – although this may be considered as an ‘early warning’. The remaining member states in the Euro-area are either subject of the corrective arm of the SGP or receive financial support.

5.2 Expenditures Benchmark

The second pillar involves an analysis of compliance with the expenditure benchmark, which is based on the ‘*Principle of prudent fiscal policy making*’, that basically curbs government expenditures to avoid that a windfall on the revenue side is being spent instead of being used for debt reduction [Regulation 1466/97][21]. A distinction is made between member states, which are ‘at or above’ their MTO and member states which are not. In the first case annual expenditure growth should not exceed a reference medium-term rate of potential GDP growth, unless the excess is matched by discretionary revenue measures. In the latter case, annual expenditure growth should not exceed a rate below the reference medium-term rate of potential GDP growth, unless the excess is matched by discretionary revenue measures[22]. In addition, any discretionary reductions of government revenue items must be matched by either expenditure reductions or by discretionary increases in other revenue items or both [Vade Mecum 2016: 48].

Figure 4: *Compliance with the Expenditures Benchmark, Euro Area* [FY 2014-2016]



Source: SCP and DBP, FY 2014-2017 [own calculations]

21. The compliance with the expenditure benchmark is not be applied when a member states has overachieved its MTO taking into account the possibility of significant revenue windfalls and the budgetary plans laid out in the stability/convergence programs [Vade Mecum 2016: 53-54].
22. The difference between the appropriate growth rate for net expenditure and the reference medium term rate of potential GDP growth is referred to as the ‘convergence margin’.

The compliance with the EB in the Euro is illustrated in Figure 4, based on in-year data and one year deviation. The number of member states in the Euro area which are compliant with the EB is growing. First the EB is not applied in four cases – Estonia, Germany Luxembourg and the Netherlands – as they are at or above their MTO, while seven other countries comply with the requirements of the preventive arm. In addition two member states in the Euro area under the preventive arm of the SGP are expected to have ‘significant deviation’ from the expenditures benchmark. The remaining member states in the Euro-area are either subject of the corrective arm of the SGP or receive financial support.

5.3 Overall Assessment

A deviation from the MTO or from the appropriate adjustment path towards is evaluated on the basis of an overall assessment [Vade Mecum 2016: 55, fn. 76], combining both indicators. The current budgetary situation of the member states in the Euro area [November 16, 2016] may be depicted as below [Figure 5].

Figure 5: *Performance of the Member States in the Euro Area under the Preventive Arm of the Stability and Growth Pact* [FY 2016][23]

EB / MTO	Compliant	Some deviation	Significant deviation	Total
Compliant	8	2	0	10
Some deviation	2	0	0	2
Significant deviation	1	0	2	3
Total	11	2	2	15

Source: DBP 2017 [own calculations]

A member state is compliant with the preventive arm if the assessment of compliance of both is positive, which happens to be eight cases. In four cases there is ‘some deviation’ and in one case ‘significant deviation’ on one indicator. The threshold is set at 0.5 of GDP as a benchmark. Finally, two countries in the Euro area – Belgium and Slovenia – are at risk of breaching the threshold of both indicators, which may lead to the start of the so-called Significant Deviation Procedure [SDP] that was introduced as part of the Six-Pack as a way of making the requirements of the preventive arm more binding[24]. Note that the ex ante overall assessment is aimed to inform the policy dialogue and cannot lead to the start of the SDP, which is triggered by the outturn ex post [Vade Mecum 2016: 32]. The remaining four countries in the Euro area are either under the corrective arm of the SGP – France, Portugal

23. The gradation in the ‘shades of grey’ refer to a color system that is ranging from blue, light blue, light purple to purple [Vade Mecum 2016: 56].
24. In case of deviation on one indicator the conclusion will be based on an in-depth analysis of the differences between the two indicators, cumulating into a decision whether the deviation can be considered significant overall.

and Spain – or receive financial support – Greece – as part of an economic adjustment program [Annex A].

However, the assessment of the performance of the member states does not account for the variation among member states. First, the MTO are tailor-made, taking into account national circumstances. The assessment of the structural balance is based on information provided by the member states and then recalculated by the Commission which often shows a minor difference[25]. The difference is not without discussion, but the forecast of the Commission is always leading as was emphasized by one of the participants. However, a member state may be in compliance with the requirements of the preventive arm of the SGP, although the MTO and/or EB are not completely up to the standards[26]. First, the structural balance is considered, as a matter of convention, to be in line with the MTO, if it is within 0.25% of GDP of its value [Vade Mecum 2016: 37]. Second, a deviation is considered to be not significant in case of an unusual event outside the control of the member state which has a major impact on the financial position of the general government or in periods of severe economic downturn for the EU as a whole or the euro area, provided that this does not endanger fiscal sustainability in the medium term [Regulation 1466/97, art. 5(1)]. The successful appeal of Italy on the 'unusual event clause' because of the consequences of the earthquake illustrates this point [Padoan, 27 October 2016]. Third, member states may invoke one of the so-called 'flexibility clauses', notably the investment clause and the structural reforms clause, including pension reforms establishing a multi-pillar system composed of a mandatory, fully funded pillar and publicly managed pillar with an associated cost to the public finances[27]. In those cases the Commission may grant a temporary deviation from the adjustment path to the MTO for a period of three years. The temporary deviation may not exceed 0.5% of GDP, except in the case of pension reforms for which there is no cap[28].

We will turn now to the design and implementation of the CSR, which are based on the overall assessment of the requirements of the preventive arm of the SGP and complete the European semester. The member states are supposed to take the CSR into account in drafting their budget for next fiscal year.

6. Country-Specific Recommendations

The consequences of the sovereign debt crisis equipped the Commission with a new tool, i.e. the authority to issue bilateral country specific recommendations, which come on top of the multilateral Broad Economic Policy Guidelines geared towards the goals of the Europe 2020 strategy. In sum, almost 745 CSR, i.e. is 4.5 per country per year, have issued so far over a period of six years [Figure 6]. As mentioned previously, we are mainly interested in the first CSR [CSR-1], which deals with fiscal consolidation [Vade Mecum 2016: 32, fn. 37], leaving

25. The deviation is due to a difference of definitions and assumptions. Besides there is a time lag between the forecast and the recalculation

26. I am grateful to one of the actors involved in the overall assessment of the performance of the member states under the preventive arm of the SGP for sharing this observation.

27. A numerical example of the flexibility clauses is given in Annex 14 of the Vade Mecum on the Stability and Growth Pact.

28. The cumulated deviation for the two clauses cannot exceed 0.75% of GDP

the CSR regarding the establishment of national budgetary frameworks out[29]. The number of CSR-1 is further narrowed down by zooming-in on the member states in the Euro area. In sum 92 CSR-1 have been made by the Council regarding fiscal reforms. The remaining CSR primarily refer to the structural reforms accounted for in the NRP, which the member states have to submit at the same time.

Figure 6: *The Number of Country-Specific Recommendations* [FY 2011-2016]

	Fiscal Reforms	Structural Reforms*	Total
Euro Area	92 [12.3%]	370 [49.7%]	462 [62.0%]
Non Euro Area	54 [7.2%]	229 [30.7%]	283 [38.0%]
Total	146 [19.6%]	599 [80.4%]	745 [100.0%]

* The number of CSR regarding structural reforms include 10 CSR on fiscal frameworks

Source: DG ECFIN [own calculations]

In its proposal for a revamped European semester, *On steps towards Completing Economic and Monetary Union*, the Commission, inter alia, introduced a greater focus by significantly decreasing the number of CSR by only covering key priority issues of macro-economic and social relevance that require attention of the member states in the up-coming twelve to eighteen months [COM(2015) 600 final: 3][30].

6.1 Design of the Country-Specific Recommendations

The second reform of the SGP, inter alia, empowered the Commission to issue CSR on the basis of the CR, followed by a policy dialogue with the member states. The outcome of that policy dialogue serves as input for the assessment of the SCP and NRP that the member states are due in the spring. Note though as one of the participants underscored that the draft CSR are no subject of the policy dialogue with the member states until they are issued by the Commission and made public. However, the draft-CSR may not come as a surprise. The priorities of the Commission are set in an early stage of the European semester. Besides, one could expect that the Commission will follow-up on CSR as long as they are not fully implemented by the member states.

A closer look at the design of the CSR-1 shows a distinct pattern over time. A typical sample of CSR-1 is composed of three elements [if applicable and relevant]:

29. The same applies to the CSR regarding taxation as well as health care and pension, although their impact on public finances is hard to ignore.
30. In addition the publication of the CSR for the Euro area is put forward so that the discussion about the CSR for the euro area takes place ahead of the discussion of the CSR per member state in order to ensure that common challenges are fully reflected in the CSR of the member states [COM(2015) 600 final: 4].

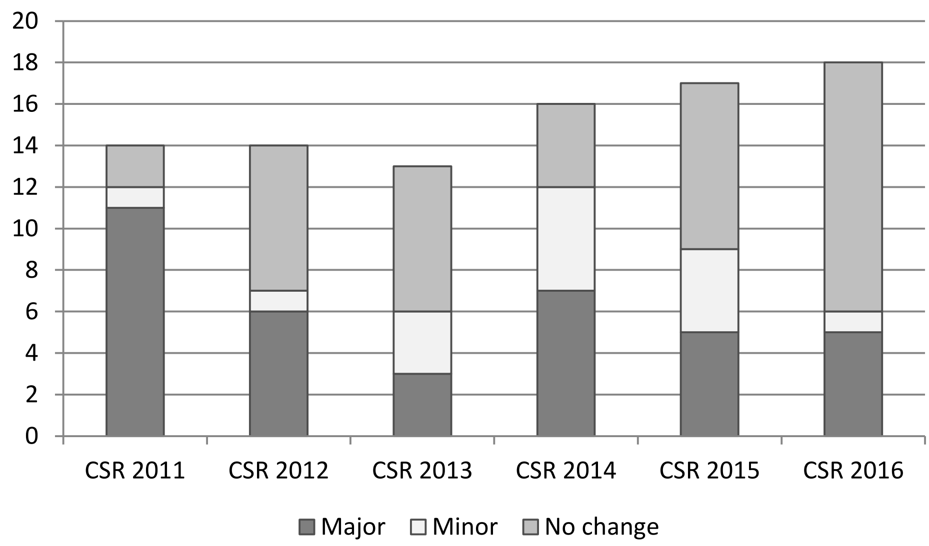
1. Preventive arm: after the correction of the excessive deficit, pursue the structural adjustment at an appropriate pace so as to reach the Medium-Term Budgetary Objective by 2015 and ensure that the high debt ratio is put on a firm downward path;
2. Corrective arm: implement the budgetary strategy in 2013 as envisaged in the Stability or Convergence Report, so as to ensure the correction of the excessive deficit by 2013;
3. Financial support: implement the measures as laid down in Implementing Decision 2011/344/EU and further specified in the Memorandum of Understanding of 17 May 2011 and its subsequent supplements.

In addition, structural measures should be ‘growth-friendly’ and the correction of the excessive deficit should be done in a ‘sustainable manner’.

The draft CSR-1 are then scrutinized by the EFC, which serves as the equivalent of COREPER in the field of fiscal affairs and is, like COREPER, composed of representatives of the member states. In addition, the Commission and the ECB are involved in the deliberations[31]. Although the meetings of the EFC are not public, one may get insight in the role of the various actors by comparing the draft text as issued by the Commission and the final version as agreed upon by the ECOFIN[32] since the Council has to follow, as a rule, the proposals and recommendations of the Commission or explain its position publicly [‘comply or explain’][33]. Consequently, the vast majority of the revisions is dealt with by the EFC and rubber-stamped by the ECOFIN as it is in the interest of all parties to avoid a confrontation.

Figure 7: *The Number of Amendments of Country Specific Recommendations in the Field of Fiscal Policy* [Euro area, FY 2011-2016].

31. The committee may meet in two different configurations i.e. with or without representatives of the national central banks.
32. The first draft of the CSR is issued by the Commission in May, followed by a bilateral and multilateral dialogue with the member states. The CSR are then discussed in the ECOFIN first in June, endorsed by European Council in July and then incorporated by governments into their national budgets and other reform plans.
33. I am one of the reviewers grateful for pointing at the legal obligation of the Council to comply or to explain. The legal basis for the ‘comply or explain’ clause can be found in Regulation 1175/2011, art. 2ab [2], which deals with the economic dialogue between the European institutions. Furthermore, a reinforced qualified majority of at least 72 percent of the member states and at least 65 percent of the population is needed when the Council does not act on a proposal from the Commission [TFEU 238, art. 3[b].



Source: SWD 2011-2016 [own calculations].

In sum, about 50 changes have been made in the CSR-1 and underlying recitals over a period of six years [2011-2016] of which only 5 are accounted for by the ECOFIN as part of the comply or explain clause[34]. All cases have to do with a disagreement of the Commission with one of the large member states, which is in line with the findings of Baerg & Hallerberg who, inter alia, conclude that large [read: more powerful] member states are more able or more likely to weaken the Commission's assessment [Baerg & Hallerberg 2016: 989]. In three cases – France, Italy and Spain – the revisions are due to the pursuit of 'horizontal consistency' in order to avoid unequal treatment of the member states. In the other two cases Germany successfully blocked a reference to a more positive fiscal stance by arguing the concept of fiscal stance is beyond the scope of the SGP and therefore cannot be imposed on the member states. However, that is not to say that small member states are less successful.

The remaining changes in the text of the CSR-1 are dealt with by the EFC which is, like the ECOFIN, aimed at reaching agreement by mutual consent[35]. The revisions may be consensual, but therefore not trivial. The findings reveal that about 40.0 percent of the CSR-1 in the Euro area has been amended substantially [Figure 7]. Besides, the changes may be characterized as a further reinforcement rather than watering down as 80.0 percent of the revisions imply a further specification and/or a quantification of the target or the horizon[36]. The outcome points at the impact of the peer pressure by the other member states, backed by the ECB, which is said to take a hawkish position. A more detailed study is needed to sort this out, but a quick scan of last year's CSR-1 shows that the Commission is still very much in the

34. The data for the CSR 2011 are not available since the 'comply or explain' clause is in force from FY 2012 onwards. In sum 48 changes have been made by the Council in the CSR over a period of 5 years [CSR 2012-2016].
35. In addition, the conclusions of the European Council and the resolutions of the European Parliament are taken into account in the final version of the CSR-1 as agreed by the ECOFIN. Contrary to the CSR regarding the NRP no other actors such as , the Economic Policy Committee, are involved in the drafting of the CSR in the field of public finances.
36. The amendments seem to correspond with the fiscal situation as the major changes primarily relate to countries in or coming out of derogation.

driver's seat in the case of fiscal policy as only 20.0% of the proposals for change submitted by one of the members of the EFC materialized in a revision of the text[37].

6.2 Implementation of the Country-Specific Recommendations

The implementation of the CSR is assessed as part of the country reports [CR] which have been issued on February 26, 2015 for the first time [38] in order to provide a single comprehensive basis for the country-specific recommendations [COM(2014) 907 final, Annex 1: 18][39]. The compliance with the CSR could be measured by the implementation index, originally design by Deroose & Griesse, making a distinction between five broad categories:

1. No progress: the member state has neither announced nor adopted measures to address the CSR. This category also applies if the member state has commissioned a study group to evaluate possible measures.
2. Limited progress: the member state has announced some measures to address the CSR, but these appear insufficient and/or their adoption/implementation is at risk;
3. Some progress: the member state has announced or adopted measures to address the CSR. These are promising, but not all of them have been implemented and it is not certain that all will be;
4. Substantial progress: the member state has adopted measures, most of which have been implemented. They go a long way towards addressing the CSR;
5. Fully implemented: the member state has adopted and implemented measures that address the CSR appropriately.

The compliance with the CSR is rather limited and uneven so far [COM(2015) 600 final: 3] as proved by the fact-sheets delivered by the staff of European Parliament that report a gradually decline of the compliance ratio from 37.5 percent [CSR 2011] to 23.5 percent [CSR 2016], cumulating into an average compliance ratio of approximately 30.7 percent. A longer time-frame may deliver a more positive compliance ratio, not in the last place because the Commission simply reiterates a CSR-1 in a somewhat different formulation if no appropriate progress is made. Finally, a CSR may be not feasible, either politically or socially[40].

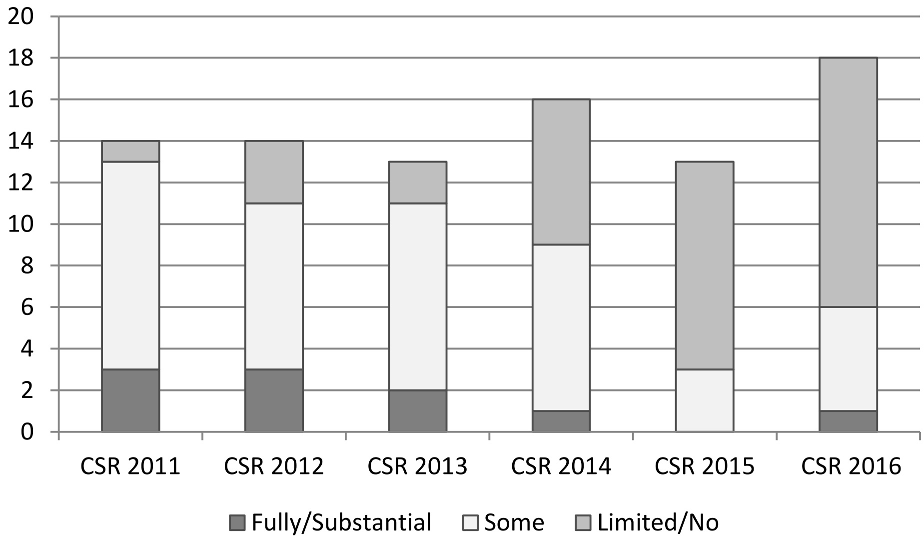
A break-down per category indicates that the compliance ratio of the CSR in the field of fiscal reforms is higher than of the CSR in the field of structural reforms[41], which may be attributed to the fact that they are subject, at least on paper, of 'hard' coordination' [Deroose & Griesse 2014: 7-8]. Similarly, the Euro area may do better than the non-Euro area: 31 vs 23 percent

37. As there are often more proposals per CSR-1, numbers may not correspond with the overall number of amendments.
38. In the past, the CR took the form of Staff Working Documents submitted by the Commission in May or June together with the draft CSR. The new publication date allows more time for discussion with the member states and other stakeholders about the final CSR [MEMO/15/4587].
39. In addition information is provided about the outcome of the In-Depth Review of 16 Member States, warranted under the Macroeconomic Imbalance Procedure [MIP].
40. As one of the participants noted, member states often upload issues for domestic consumption or symbolic reasons .
41. The compliance ratio of the CSR regarding fiscal reforms [44.0%] outnumbers the CSR structural reforms [29.0%]. The same applies for the CSR in the field of macro-economic imbalances, [Darvas & Leandro 2015: 2].

[Darvas & Leandro 2015: 6-7][42]. In this paper we zoom-in on the implementation of the CSR in the field of fiscal reforms in the Euro-area, the main reason being that the Two-Pack is only applicable to those countries that adopted the single currency. We apply more or less the same methodology looking at the evolution of the compliance ratio over a longer period of time[43]. The outcome shows that the implementation of the CSR-1 is gradually diminishing, making it hard to assess the impact of the CSR-1, if any, on fiscal consolidation.

A cross-national comparison of the implementation of the CSR-1 reveals that in 6 cases no CSR-1 has been issued regarding the SCP because a member state is at or above its MTO and in 15 cases because a member state is receiving financial support as part of an economic adjustment program. Furthermore, there is no distinct pattern – neither per country, nor over time – or it should be that all countries are in the same league, ranging somewhere in between 'limited progress' and 'some progress', with Finland as the only exception [see Annex B][44].

Figure 8: *The Compliance with the Country-Specific Recommendations in the Field of Fiscal Policy* [Euro Area, FY 2011-2016].



Source: SWD 2011-2014, CR 2015-2016 [own calculations]

Last but not least, a more detailed and refined analysis is needed to sort-out the exact impact of fiscal reforms as the CSR-1 refers to the broader concept of public finances. However, the Commission 'fiddled around' with the concept of public finances as subtly noted by one of the participants. On top of the requirements of the SGP, it could refer to fiscal frameworks, which are sometimes included and sometimes excluded from the CSR-1, as well as to structural reforms, such as health care system and pension reforms. Admittedly, these expenditure categories may have a substantial impact on fiscal consolidation, notably in the long run, but they blur a longitudinal analysis of fiscal reforms. Besides, the compliance with the

42. The analysis by Darvas & Leandro is limited their analysis to the 21 countries [14 Euro area, 7 non-Euro area] for which data were available for all years. Contrary to Deroose and Griesse they use a 3-points scale by combining the first two categories and last two categories in order to take the implementation of the CSR 2011 also into account [Darvas & Leandro 2015: 5].
43. The scores are adjusted for the accession to the Euro area and controlled for missing data.
44. The same applies to both other Scandinavian countries – Denmark and Sweden – as we broaden the scope to the EU as a whole.

requirements of the SGP is no longer assessed as part of the CR, but as part of the SCP in the spring[45]. Consequently, the compliance ratio of the CSR-1 basically limited to the implementation of the non-SGP components of public finances. As illustrated by the case of Austria, a member state can be 'broadly compliant' with the SGP, although it made only 'limited progress' towards its CSR-1 at the same time [European Commission 2016c: 21-22].

7. Conclusion

The response of the European Union to the sovereign debt crisis constitutes an integration paradox [Puetter 2012; 168; Van Nispen & Rijk 2014: 16]. On the one hand, we feature a revival of intergovernmentalism or 'new-intergovernmenalism' [Bickerton et al. 2015] as the Commission was largely sidelined by Taskforce on Economic Governance. On the other hand, we may argue that the outcome of the Taskforce is breathing supranationalism as the Commission is equipped by all kinds of new instruments. First and foremost, the latest reform of the SGP brought the 'a European Semester for better ex-ante integrated fiscal policy coordination' [COM (2010) 250: 9]. Second, the Commission issued the Six-Pack that basically codified the European semester. It has been heavily scrutinized by European Parliament, but the outcome was a stronger role to the Commission at the expense of the Council throughout new processes of oversight of budget and wider economic policy planning [Phillips 2011][46]. The struggle for power is finally settled in favor of the Commission by the adoption of the Two-Pack, backed-up by the Fiscal Compact that directs the coordination of the budgetary policy of the member states. The compliance with the requirements of the SGP leaves the Commission with strong discretion, as does its role as an information hub between the member states in the coordination of budgetary policy [Bauer & Becker 2014: 226]. To put it differently, the Commission acquired more power indeed, but that power is deliberately granted by the member states. It seems safe to conclude that the 'integration paradox' ended-up in new supranationalism [Dehousse 2015; Schmidt 2017] rather than in new intergovernmentalism, at least in the field of European fiscal governance,

In this paper we looked at the reform of the SGP regarding the coordination of budgetary policy and, more precisely, at the impact of the CSR on fiscal consolidation. The findings are somewhat mixed. At the moment 15 out of 19 countries in the Euro area are under the preventive arm of the SGP of which 8 are compliant with both pillars – MTO and EB – of the overall assessment of fiscal performance [Annex A][47]. At the moment the situation in two countries in the Euro area – Belgium and Slovenia – is at risk of non-compliance. Unfortunately, it is still largely unclear if fiscal consolidation may be attributed to the measures that have been taken to reinforce European fiscal governance. First, the causal relationship of the compliance with CSR-1 and the assessment of fiscal consolidation is pretty much obscure. The compliance with the CSR-1 serves as input for the policy dialogue of the Commission with the member states. The outcome is taking into account by the Commission in the assessment of the SCP as part of the European semester. Second, the implementation ratio of the CSR-1 may be simply too low to have impact on fiscal consolidation. So, it seems

45. The assessment of the CSR-1 is referred in four cases – Estonia, Finland, Latvia and Malta – to the assessment of the SCP in the spring. Unfortunately, the methodology used in the CR and SCP is not compatible.
46. In sum, more than 2000 amendments have been made by European Parliament in order to strengthen the position of the Commission as the guardian of the treaty.
47. The same applies to Sweden that stayed outside the Euro area.

to be safe to conclude that other factors, such as the fiscal rules of the SGP and GDP [Molnár 2012: 126] are at play than the implementation of CSR-1 by the member states.

Finally, one may question if the relative low compliance ratio is only due to either a policy or institutional misfit between both levels of economic governance or that compliance with the CSR-1 is hindered by lack of facilitating factors for domestic change, such as institutional support or the lack of veto points [Börzel & Risse 2003]. At least two observations can be made. First, it does not really help that the CSR are not legally binding. It leaves the compliance with the CSR-1 to the discretion of the member states, although it will be difficult them in the long run unless the economy recovers. One may question though if legally binding CSR would make any difference, given the experience in the past with other tools of European fiscal governance. However, the color scheme, mirroring a traffic light, introduced in the overall assessment of both the MTO and EB seems to work. The member states stretch the margins as much as possible, but do their utmost best with the help of a computer program not to end in the red zone [= significant deviation]. Second, the implementation of CSR-1 largely mirrors the interplay between 'guardians' and 'advocates' of the budget at the national level, making the implementation of the CSR-1 largely dependent on the position of the Minister of Finance vis-à-vis the line ministers.

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Annex A: Compliance to the Preventive Arm of the Stability and Growth Pact [Euro Area, FY 2016]

Preventive Arm*		**MTO**		**EB**		**OA**
1	Austria	0.0		0.6		C
2	Belgium	-0.7		-1.4		SD
3	Cyprus	0.2		2.1		C
4	Estonia	C		C		C
5	Finland	-0.5		0.2		OA
6	Germany	C		C		C
7	Ireland	-0.5		0.1		OA
8	Italy	-0.2		0.3		OA
9	Latvia	0.2		-0.3		OA
10	Lithuania	0.4		0.4		C
11	Luxembourg	C		C		C
12	Malta	0.5		0.6		C
13	Netherlands	C		C		C
14	Slovakia	0.1		-0.1		OA
15	Slovenia	-0.8		-0.5		SD

Source: DBP 2017

Explanatory note

Compliance

Some Deviation

Significant Deviation

Acronyms

C = Compliance

OA = Overall Assessment

SD = Significant Deviation

Annex B: The Amendments and Compliance of the Country-Specific Recommendation on Fiscal Consolidation [Euro Area, FY 2011-2016]

	Country	Total	CSR-1[1]	Amendments	Compliance
1	Austria	31	6	2.3	2.8
2	Belgium	33	6	2.5	2.5
3	Cyprus	19	3	2.0	2.7
4	Estonia	24	6	2.5	2.8
5	Finland	27	6	3.2	3.8
6	France[2]	34	6	3.5	2.5
7	Germany	22	6	2.5	2.8
8	Greece[3]	N/A	N/A	N/A	N/A
9	Ireland	14	3	2.3	2.7
10	Italy	37	6	3.5	2.5
11	Latvia	12	3	1.0	2.5
12	Lithuania	6	2	1.0	2.5
13	Luxembourg	25	6	1.7	2.5
14	Malta	27	6	2.0	2.6
15	Netherlands	23	6	2.0	2.8
16	Portugal[2]	18	3	3.3	2.7
17	Slovakia	32	6	1.3	2.7
18	Slovenia	38	6	2.8	2.5
19	Spain[2]	40	6	3.7	2.5
		462	**92**	**2.3**	**2.5**

1. The number of CSR-1 regarding the requirements of SGP.
2. Excessive Deficit Procedure
3. Economic Adjustment Program

Annex C: Methodological Note

1. The Overall Assessment

The overall assessment of the fiscal performance of the member states in the Euro area under the preventive arm of the SCP, which combines the compliance with the MTO and the EB, is done on the basis of the assessment of the SCP and DBP that the member states have to submit in the spring, respectively the fall. The data provided by the member states are recalculated by the Commission on the basis of a commonly agreed definition. In this paper we use the data from the Commission because of analytical reasons and internal coherence.

The performance of the member states is structured in three rather broad categories:

1. Compliant, i.e. a structural deficit which is within a granted margin 0.25% of GDP of its value;
2. Some deviation, i.e. any deviation which is *not* significant;
3. Significant deviation, i.e. a deviation of more than 0.5% of GDP in one year or an average deviation of 0.25% of GDP over two years[48].

The assessment of the SCP and DBP provide data for at least three consecutive years: previous year [t-1], current year [t] and next year [t+1]. We focus on the data for current year [in-year], i.e. the data of FY 2016 in the case of the DBP 2017, which have been published on November 16, 2016. As for the deviation from the required adjustment path to the MTO as well as from the EB we refer to one year, which is set at 0.5 % of GDP[49].

2. The Design of the CSR

As for the design of the CSR, the draft text issued by the Commission is compared with the final text as adopted by the Council. The data are taken from the CSR 2011-2016[50] as summarized in the fact-sheets provided by the EP/ECON-staff.

The analysis of the revisions of the CSR is composed of six subsequent steps:

1. A comparison of the draft text as issued by the Commission and the final text as adopted by the Council;
2. Taking stock of all editorial changes;
3. The assessment of the editorial changes on a 5-points scale, ranging from no change [1] to substantial change in terms of further specification in quantitative terms [5];

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48. Note that a deviation may be considered to be not significant in the case of exceptional circumstances or flexibility clause.

49. A deviation from the require adjustment path to the MTO is considered to be significant when the change in the structural balance if the deviation is at least 0.5% of GDP in a single year or at least 0.25% of GDP on average per year in two consecutive years. The same applies to a deviation from the expenditure benchmark.

50. A similar approach is followed by Baerg & Hallerberg [2016] looking , inter alia, the weakening of the CSR and therefore, undermining of the watchdog function of the Commission by the large member states [Baerg & Hallerberg 2016].

4. Sorting out the editorial changes agreed upon by the EFC[51] and rubber-stamped by the ECOFIN and the editorial changes made by the Council as accounted for by the 'comply or explain' clause;
5. Zooming in on the major editorial changes in both qualitative as quantitative terms [category 4 and 5];
6. Analysis of the major editorial changes in terms of reinforcement or watering down of the original proposal.

The 5-points scale is later reduced to a 3-points scale making a difference between no or limited progress [combining category 1 and 2], some progress [category 3] and major progress [combining category 4 and 5] to enable a comparison of the findings with the outcome of other studies [Deroose & Griesse 2014; Darvas & Leandro 2015].

3. The Implementation of the CSR

The implementation of the CSR basically follows the methodology applied by the Commission, making a difference between 5 broad categories:

1. No progress: the member state has neither announced nor adopted measures to address the CSR. This category also applies if the member state has commissioned a study group to evaluate possible measures.
2. Limited progress: the member state has announced some measures to address the CSR, but these appear insufficient and/or their adoption/implementation is at risk;
3. Some progress: the member state has announced or adopted measures to address the CSR. These are promising, but not all of them have been implemented and it is not certain that all will be;
4. Substantial progress: the member state has adopted measures, most of which have been implemented. They go a long way towards addressing the CSR;
5. Fully implemented: the member state has adopted and implemented measures that address the CSR appropriately.

The 5-points scale is later reduced to a 3-points scale making a difference between no or limited progress [combining category 1 and 2], some progress [category 3] and major progress [combining category 4 and 5] to enable a comparison of the findings with the outcome of other studies [Deroose & Griesse 2014; Darvas & Leandro 2015]. The data are taken from the Country Reports [previously Staff Working Documents], which are published in February from 2015 onwards.

4. Interviews

A series of open interviews is conducted on January 17-20, 2017 with officials from the Secretariat-General of the Council of Ministers [3], the Secretariat-General and Directorate-General for Economic and Financial Affairs [DG ECFIN] of the European Commission [5] and the staff of the Economic and Monetary Affairs [ECON] committee in European Parliament [2].

51. The Economic and Financial Committee [EFC] is the equivalent of COREPER in the field of public finances.